09/13/96

UNITED STATES DISTRICT COURT

WESTERN DISTRICT OF LOUISIANA

SHREVEPORT DIVISION

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CRYSTAL OIL COMPANY AND CRYSTAL EXPLORATION AND PRODUCTION COMPANY, Plaintiffs,	§	CASE NO. CV95-2115S
vs.	§	JUDGE STAGG
ATLANTIC RICHFIELD COMPANY, Defendant.	§	MAGISTRATE JUDGE PAYNE

DEFENDANT'S REPLY MEMORANDUM IN SUPPORT OF STATEMENT OF APPEAL AND MOTION FOR MANDATORY WITHDRAWAL OF REFERENCE

MAY IT PLEASE THE COURT:

Defendant, ATLANTIC RICHFIELD COMPANY ("ARCO" or "defendant"), has filed its Statement of Appeal and Memorandum in support thereof from the Order of Severance and Referral to Bankruptcy Court (the "Referral Order") and the Memorandum Ruling supporting the Referral Order issued by Magistrate Judge Payne on July 19, 1996. The issue referred to the bankruptcy court was the declaration sought by plaintiffs, CRYSTAL OIL COMPANY ("Crystal" or "plaintiff") and CRYSTAL EXPLORATION AND PRODUCTION COMPANY ("CEPCO" or plaintiff"), that ARCO's claim against Crystal under the Comprehensive Environmental Response, Compensation, and Liability Act of 1980, 42 U.S.C. §§ 9601, et seq. ("CERCLA"), was discharged through Crystal's 1986 Chapter 11 bankruptcy case (the "Bankruptcy Discharge Issue"). ARCO has also filed a Motion to withdraw reference of the Bankruptcy Discharge Issue from the

53

bankruptcy court. This Reply Memorandum is filed in support of ARCO's Statement of Appeal and its Motion for Mandatory Withdrawal of Reference. In Crystal's response to ARCO's Motion for Mandatory Withdrawal of Reference, it simply attached a copy of its Memorandum in Opposition to ARCO's Appeal. The issues involved in the ARCO's Appeal and in the Motion for Withdrawal of Reference are the same.

Crystal asserts that resolution of the Bankruptcy Discharge Issue is a simple and straightforward question of bankruptcy law, relying principally upon In re Chateaugay Corp., 944 F. 2d 979 (2d Cir. 1991), and LTV Steel Co., Inc. v. Union Carbide Corp. (In re Chateaugay), 193 B.R. 669 (S.D.N.Y. 1996). The underlying facts in Chateaugay, which Crystal failed to discuss, are important in understanding ARCO's position here. The debtor, LTV Corporation ("LTV"), had listed in its schedule of liabilities 24 pages of "contingent" environmental liabilities or claims that were held by, inter alia, the Environmental Protection Agency ("EPA"). The EPA filed a proof of claim for approximately $32 million, representing response costs incurred pre-petition. LTV informed the EPA that it expected confirmation of a reorganization plan to discharge all obligations of LTV concerning environmental liabilities that were traced to pre-petition conduct of the debtor, including obligations for response costs that were incurred post-confirmation. The EPA disagreed with that position and brought an adversary proceeding for a declaratory judgment that response costs incurred "post-confirmation" were not dischargeable

because they did not arise from pre-petition claims. The government contended that it did not have a "claim" within the meaning of the Bankruptcy Code for reimbursement of CERCLA response costs until those costs had been actually incurred. The Second Circuit held that response costs incurred by the EPA were pre-petition claims that were dischargeable in bankruptcy regardless of when the costs were incurred or that the EPA did not yet know the full extent of costs that might one day be incurred. Essentially, the court's entire focus was whether CERCLA costs constituted a "claim" and when that claim was deemed to have arisen.

Likewise, in LTV, the CERCLA issues presented were whether the CERCLA actions constituted bankruptcy "claims," and if so, when the claims arose. Recognizing that these issues had been decided in Chateaugay, the court relied on Chateaugay's "accrual rule" and denied withdrawal of reference. However, and significantly, the court made the following statement:

> Had the underlying proceeding raised substantive CERCLA issues, such as whether LTV is at all liable for the toxic site and its clean-up, the inquiry might be different, but defendants here have not identified any other CERCLA issues in this case.

LTV, 193 B.R. at 674 (emphasis added).

The case before this Court does not involve the simple question of when a release of hazardous substances took place or whether ARCO's CERCLA counterclaim is indeed a "claim" under the Bankruptcy Code. The CERCLA issues that must be decided in this case were not decided by Chateaugay or LTV, nor any other case cited by Crystal. As discussed in ARCO's Memoranda in support of

its Statement of Appeal filed August 2, and in support of its Motion for Mandatory Withdrawal of Reference filed August 9, the Bankruptcy Discharge Issue involves resolution of substantial and material questions of Title 11 and non-bankruptcy code federal law, i.e., "substantive CERCLA issues." At a minimum, the following questions must be resolved under CERCLA:

1. Could a CERCLA Claim Truly be Contemplated in 1986 for an Ongoing Mining Site?

CERCLA claims contemplate the recovery of cleanup costs for abandoned sites or facilities. See, e.g., Acme Printing Ink Co. v. Menard, Inc., 870 F. Supp. 1465, 1475 (E.D. Wis. 1994) ("CERCLA was designed to force the cleanup of abandoned hazardous waste sites that pose some risk to public health or the environment"). Thus, an important CERCLA question that must be resolved here is whether the RICO mining site, still owned by ARCO in 1986, was such an "abandoned" facility at that time, or whether it was properly characterized as a potentially active mining site subject to cleanup under Colorado permitting and reclamation laws. In the latter circumstance, only the current owner/operator can be held responsible for cleanup costs, see C.R.S. §§ 34-32-101, et seq., leaving ARCO with no avenue in 1986 to pursue a CERCLA claim against Crystal or any other party.

2. Could ARCO, in 1986, Have Contemplated a CERCLA Claim Against Crystal When it Was CEPCO that Previously Owned the Property?

Another important CERCLA question to be resolved here is whether ARCO should have fairly contemplated in 1986 under then

existing CERCLA law that it would have had any such CERCLA claim against Crystal, the parent corporation of CEPCO, when the RICO property was purchased from CEPCO and not Crystal? Stated differently, if ARCO had a claim against CEPCO under CERCLA in 1986, did that claim equate to a claim against Crystal such that ARCO should have filed a proof of claim in the Crystal bankruptcy proceeding? The answers to these questions require interpretation of CERCLA as the courts understood the statute in 1986. This area of CERCLA law was particularly unsettled in 1986, and remains so to this day. Courts have taken widely divergent approaches to assessing the nature and level of control required to invoke corporate shareholder liability under CERCLA, as reflected in the contrasting tests adopted by this Court in Joslyn Mfg. Co. v. T.L. James & Co., Inc., 696 F. Supp. 222 (W.D. La. 1988), aff'd, 893 F. 2d 80 (5th Cir. 1990) (applying the traditional veil piercing approach) and by other circuit courts, see, e.g., U.S. v. Kayser-Roth Corp., Inc., 910 F. 2d 24 (1st Cir. 1990) (adopting a broad "control" test for operator liability). Thus, the question of whether ARCO should have fairly contemplated a CERCLA claim against Crystal really boils down to a thorny CERCLA issue: How interwoven need Crystal have been with CEPCO, and/or the RICO site itself, for ARCO to have been vested with knowledge of the claim against the parent?

3. What is the Status of a Site Under CERCLA When EPA Takes an Initial Look at it, Then Decides Not to Include it in the Superfund Program?

EPA has set regulatory procedures for assessing the incredibly broad universe of sites that potentially may meet CERCLA's basic criteria for inclusion in the Superfund program, and then weeding out those sites that do not deserve such a dubious distinction. See 40 C.F.R. § 300, et seq. (known as the National Contingency Plan ("NCP")). This is exactly what happened at the RICO site: EPA conducted a very preliminary review of the site in 1985, and concluded that it did not merit further scrutiny at that time, in part because ARCO was present at the site. A significant legal and policy issue arises in these circumstances as to whether a private party should be vested with knowledge of, and be required to pursue, a CERCLA claim, notwithstanding the agency's determination that cleanup resources are better directed to other sites. Resolution of this issue requires an evaluation of EPA's Superfund site designation procedures under the NCP, a strictly CERCLA-esque (and somewhat tortuous) process. Again, this type of analysis lies outside the typical provence of the bankruptcy court.

4. Given How CERCLA Was Perceived and Developed in 1986, Could ARCO Really Have Foreseen Its Application to the Rico site?

This case requires the Court to travel back in time one decade in order understand how differently CERCLA was perceived and applied in 1986. The distinction between the statute as currently

applied and its status in the mid-1980s was emphasized in another recent decision:

> And, in fact, CERCLA was a sleeper at first. It was widely thought to be a short-range law; it had a self-destruct provision of September 30, 1985. Prior to reauthorization in 1985, it had accomplished long-term total cleanup of only 14 sties. Furthermore, the political climate was not conducive to bold environmental initiatives. The EPA administrator appointed in 1981 was reluctant to use the full authority provided by the Act. She and other top administrators wanted to limit the program to five years, and they minimized the extent of hazardous waste problems.

In Re Chicago, Milwaukee, St. Paul & Pacific R.R. Co., 78 F. 3d 283, 289 (7th Cir. 1996). As this decision aptly points out, to resolve whether ARCO should have known of the Crystal claim in 1986 under CERCLA requires the Court to fully understand the drastic changes in the policies, caselaw and application of CERCLA that have occurred over the last decade, triggering substantial and unsettled CERCLA issues.

Numerous other examples of CERCLA issues which permeate this matter could be cited. In short, CERCLA cases are fraught with messy and often unresolved CERCLA issues, and this case is a prime example.[1]

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[1] Notwithstanding these unsettled CERCLA issues, Crystal argues that the law in the Fifth Circuit on the bankruptcy-CERCLA interplay issue is well settled, citing Lemelle v. Universal Mfg Corp., 18 F. 3d 1268 (5th Cir. 1994). However, in this products liability case, the court did not have before it the issue of contingent environmental liabilities, much less the significant CERCLA questions discussed above. Indeed, the court was dealing with whether the definition of the word "claim" could be extended to include the plaintiffs in product liability claims who were completely unknown and unidentified at the time of the filing of the bankruptcy petition. The court carefully explained at the conclusion of the opinion that it was deciding nothing else. Id. at 1278.

CONCLUSION

ARCO, in its Memorandum in Support of the Motion for Mandatory Withdrawal of Reference at 3-7, illustrates that the various federal district courts, bankruptcy courts and courts of appeal have employed widely varying and inconsistent standards for determining when a CERCLA claim arises for purposes of bankruptcy. Plaintiffs allege in response that these standards are actually well settled. Regardless of how the Court views this issue, it is clear that the unique circumstances presented in this case engender a host of CERCLA issues that go beyond the assessment of when a generic "claim" arises. As such, this matter easily meets the test adopted in In Matter of LAJET, Inc., 1995 W.L. 72428 (E.D. La. 1995): "[T]he proceeding will require significant interpretation and substantial material consideration of CERCLA. Since CERCLA has been held to initially 'affect interstate commerce' for these purposes, see United States v. ILCO, Inc., 48 B.R. 1016, 1021 (N.D. Al.), withdrawal of reference is mandatory."

For these reasons, Magistrate Judge Payne's Referral Order should be vacated and ARCO's Motion for Mandatory Withdrawal of Reference should be granted, and the Bankruptcy Discharge Issue should be returned to this Court for decision.

Shreveport, Louisiana, this 13th day of September, 1996.

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CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the above and foregoing Defendant's File Reply Memorandum in Support of Statement of Appeal and Motion for Mandatory Withdrawal of Reference has been served upon plaintiffs' counsel of record, Osborne J. Dykes, III, Fulbright & Jaworski, 1301 McKinney, Suite 5100, Houston, Texas 77010-3095, and Albert M. Hand, Jr., Cook, Yancey, King & Galloway, P.O. Box 22260, Shreveport, Louisiana 71120-2260, by depositing a copy of same in the U.S. Mail, properly addressed, with adequate postage affixed thereto.

Shreveport, Louisiana, this 13th day of September, 1996.

OF COUNSEL